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REPORT TO THE LEGISLATURE

DEPARTMENT OF STATE LANDS

Financial-Compliance Audit for the

Two Fiscal Years Ended June 30, 1987

This report contains six recommendations for improvement of the department's operations. The major items addressed in this report include:

- Lost Interest Revenue
- Unrecorded General Fund Revenue
- Fire Suppression Funding
- Unpaid Insurance Premiums

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FINANCIAL-COMPLIANCE AUDITS

Financial-compliance audits are conducted by the Office of the Legislative Auditor to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations which could have a significant financial impact. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office.

Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

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STATE OF MONTANA

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April 1988

The Legislative Audit Committee
of the Montana State Legislature:

This is the financial-compliance audit report on the Department of State Lands for the two fiscal years 1985-86 and 1986-87. Included in this report are recommendations concerning lost interest revenue, unrecorded General Fund revenue, fire suppression funding, and unpaid insurance premiums. The department's written response to audit recommendations is included at the end of the audit report.

We thank the commissioner and his staff for their cooperation and assistance throughout the audit.

Respectfully submitted,

Scott A. Seacat
Legislative Auditor

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Office of the Legislative Auditor

DEPARTMENT OF STATE LANDS

Financial-Compliance Audit for the
Two Fiscal Years Ended June 30, 1987

Audit staff involved in the Department of State Lands audit included: Wayne Kedish, Wayne Guazzo, Bill O'Donnell, Paul Christofferson, Renee' Foster, and Geri Huschka.

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DEPARTMENT OF STATE LANDS

ELECTIVE AND ADMINISTRATIVE OFFICIALS

STATE BOARD OF LAND COMMISSIONERS

Ted Schwinden, Chairman	Governor
Ed Argenbright	Superintendent of Public Instruction
Andrea "Andy" Bennett	State Auditor
Jim Waltermire	Secretary of State
Mike Greely	Attorney General

ADMINISTRATIVE OFFICIALS

Dennis Hemmer	Commissioner
James Williams	Administrator Central Services Division
Gary Brown	Administrator Forestry Division
Kelly Blake	Administrator Land Administration Division
Gary Amestoy	Administrator Reclamation Division
Randy Mosley	Administrator Field Operations

SUMMARY OF AUDIT RECOMMENDATIONS

The following is a listing of recommendations from our financial-compliance audit of the Department of State Lands.

	Page
Recommendation #1 The department continue to request advance payments from the federal government.	4
Agency Response: Concur. See page 22.	
Recommendation #2 The department record all expenditures and liabilities for insurance premiums in the year incurred.	5
Agency Response: Concur. See page 22.	
Recommendation #3 The department: A. Prepare federal billing statements in a timely manner.	6
B. Recognize revenue in accordance with state accounting policy.	6
Agency Response: Concur. See page 23.	
Recommendation #4 The department develop an improved method of funding fire suppression costs incurred at the end of a biennium.	8
Agency Response: Concur. See page 23.	
Recommendation #5 The department adopt a plan to restore the trust and legacy fund corpus as required by state policy.	9
Agency Response: Concur. See page 23.	
Recommendation #6 The department establish procedures to ensure federal reports are accurate.	10
Agency Response: Concur. See page 23.	

INTRODUCTION

We performed a financial-compliance audit of the Department of State Lands (DSL) for the two fiscal years ended June 30, 1986 and 1987. The objectives of the audit were to:

1) Determine if the department's financial schedules present fairly the results of its operations for the two fiscal years ended June 30, 1986 and 1987;

2) Determine if the department complied with applicable laws and regulations;

3) Review the adequacy of the management information systems and make recommendations for improvement in the department's administration and accounting controls; and

4) Determine the implementation status of prior audit recommendations.

This report contains six recommendations to the department. These recommendations address areas where the department can improve systems, financial reporting, and compliance with laws and regulations. Other areas of concern deemed not to have a significant effect on the successful operations of the department are not included in this report but have been discussed with management.

In accordance with section 5-13-307, MCA, we analyzed and disclosed the costs, if significant, of implementing recommendations.

BACKGROUND

The Department of State Lands (DSL) was created in 1927 and was reorganized in its present form by Chapter 529, Laws of 1981. The Board of Land Commissioners is constitutionally created to act as the department head. The board consists of the Governor, the Superintendent of Public Instruction, the State Auditor, the Secretary of State, and the Attorney General. The land commissioner is appointed by the Governor, subject to Senate approval, and under the direction of the Board of Land Commissioners, serves as the chief administrative officer.

Under the board's direction, the department is responsible for the care, management, and disposition of state lands. DSL collects and receives all moneys payable to the state as fees, rentals, royalties, interest, penalties or

payments on mortgages, purchases, or leases of lands administered by the department.

The department employed approximately 300 FTE, and spent approximately $19,132,000 and $18,111,000 in budgeted program expenditures during fiscal years 1985-86 and 1986-87, respectively. Total budgeted revenue collected during fiscal years 1985-86 and 1986-87 was approximately $55,537,000 and $46,898,000, respectively.

The department's activities are organized under five divisions, each headed by an administrator:

Centralized Services Division - performs the overall administrative services for the department. The division processes trust income received from surface and subsurface leases for school trust funds. Other responsibilities include administration of grants from the U.S. Office of Surface Mining, and the U.S. Forest Service. The division administers the department's aviation operation and coordinates the department's data processing activities.

Land Administration Division - responsible for the appraisal and classification of all state lands. The division's objective is to obtain the greatest revenue for the trust funds commensurate with the preservation of the resource. The division also administers mineral leases for school trust funds.

Reclamation Division - regulates all mining-related surface disturbances in the state.

Forestry Division - responsible for state trust lands which are principally valuable for timber, for the growing of timber, or for watershed protection. The division provides for fire suppression efforts on state and private lands.

Field Operations Division - responsible for operations carried out in the various field and land offices throughout the state. Operations in the field offices include forestry and land management tasks.

SUMMARY OF PRIOR AUDIT RECOMMENDATIONS

The financial-compliance audit of the Department of State Lands for the two fiscal years ended June 30, 1985 contained ten separate recommendations directed to the department. Eight of these recommendations are still applicable. We reviewed the status of these recommendations with the following results:

Implemented	Partially Implemented	Not Implemented	Total
5	1	2	8

The recommendations which have not been implemented relate to fire suppression funding and bond swaps as discussed on pages 7 and 8, respectively. The recommendation partially implemented concerned the Montana Natural Areas Act of 1974 and has been discussed with department management.

LOST INTEREST REVENUE

During its participation in federal agricultural programs, the department did not request optional advance payments from the federal government. Receipt of advance payments would have provided additional interest earnings for the related trust accounts. By not requesting advance payments from the federal government, the department lost potential interest earnings.

The federal Food Security Act of 1985 (the 1985 farm bill) reduces the production of commodities by offering price and income support payments to land owners. The support payments are offered to eligible crop producers through the United States Department of Agriculture (USDA) Price Support and Production Adjustment Program. Participants in the program are required to designate the portion of their acreage to be taken out of production and devoted to conservation uses (Acreage Conservation Reserve "ACR") and the acreage on which a crop may be planted (permitted acreage). Program participants receive a diversion payment for the acreage taken out of production. For an eligible crop grown on permitted acreage, the producer and/or the land owner will earn a deficiency payment for the difference between the program's target price per bushel and the national average loan rate per bushel. Beginning in 1986, the producer and the department (the land owner) could request 40 percent of eligible deficiency and diversion payments in advance when enrolling in the program. Prior to 1986, the producer and the department could have requested 50 percent of eligible deficiency and diversion payments in advance.

State lands leased for agricultural purposes are eligible for enrollment in the Price Support and Production Adjustment Program. When enrolling in the

program, the department currently has the option of requesting the advance payment of 40 percent of its share of the total deficiency and/or diversion payment. The department's share of the total payment is at least 25 percent. This percentage is the same percentage that would be received for a harvested crop on state leased land not enrolled in the program.

In calendar years 1984, 1985, and 1986, the department did not request the allowable advance payments for state lands enrolled in the Price Support and Production Adjustment Program. If the department had collected the advance payments, the state would have earned an estimated $139,820 in interest revenue in the three calendar years ended December 31, 1986. If additional expenses were incurred to properly process the advance payments, we believe the costs would have been significantly less than the additional investment revenue.

Since we pointed out that the state lost a significant amount of interest revenue, the department began requesting the advance payments in calender year 1987.

RECOMMENDATION #1

WE RECOMMEND THE DEPARTMENT CONTINUE TO REQUEST ADVANCE PAYMENTS FROM THE FEDERAL GOVERNMENT.

UNPAID INSURANCE PREMIUMS

The department did not comply with section 17-1-102(4), MCA, which requires it to record all liabilities and expenditures on its financial records in accordance with procedures prescribed by the Department of Administration. The Department of Administration has prescribed procedures for recording liabilities and expenditures which are explained in the Montana Operations Manual. State law also requires agencies to apply Generally Accepted Accounting Principles (GAAP) in its financial accounting. GAAP accounting requires expenditures to be recorded in the year the obligation is incurred.

Under state law, the Department of Administration is responsible for the acquisition and administration of all the insurance purchased for protection of the state. For the two fiscal years ended June 30, 1987, the Department of State Lands budgeted for the costs of helicopter, aircraft, and auto insurance

premiums based upon estimates provided by the Department of Administration. The actual bids subsequently received and accepted by the Department of Administration were for up to twice the budgeted amounts. Since the Department of State Lands had not budgeted for the unanticipated increase, the department only paid the amounts it had budgeted. By recording only the amounts budgeted for insurance premium expenditures, the department understated General Fund expenditures and liabilities by $12,967 in fiscal year 1985-86 and by $27,697 in fiscal year 1986-87.

In fiscal year 1985-86, the department had sufficient spending authority to record the expenditure, since at fiscal year-end, $79,781 remained in the department's General Fund appropriation. However, based on the department's actual fiscal year 1986-87 expenditures, if the department had included the entire cost of the insurance premiums for the fiscal year 1986-87, the department would have overspent its General Fund appropriation by $3,970. State law requires that agencies not exceed their appropriation authority.

Department officials indicated that because the Department of Administration significantly underestimated the cost of insurance premiums, it was not possible for the Department of State Lands to accurately budget for insurance premiums in fiscal years 1985-86 and 1986-87. As a result, the Department of State Lands chose to only pay the amounts they had budgeted.

Regardless of whether the entire cost of the insurance premiums were budgeted, the total insurance costs represented a valid obligation of the department. Therefore, the entire cost of the insurance premiums should have been recorded as expenditures and liabilities in the year the obligations were incurred, as required by state law.

RECOMMENDATION #2

WE RECOMMEND THE DEPARTMENT RECORD ALL EXPENDITURES AND LIABILITIES FOR INSURANCE PREMIUMS IN THE YEAR INCURRED.

UNRECORDED GENERAL FUND REVENUE

We noted federal reimbursement for fire suppression costs incurred by the Forestry Division are not recorded in the proper fiscal year. State firefighters

assisted the federal government in fire suppression during the summer of 1986 (fiscal year 1986-87). The state incurred costs that were subject to federal reimbursement. To obtain reimbursement, it was necessary for the Forestry Division to prepare and send a billing statement to the U.S. Forest Service. During fiscal year 1986-87, the division did not bill the U.S. Forest Service for the fire suppression costs incurred during the summer of 1986 and, did not accrue revenue at fiscal year-end 1986-87. A department official indicated the forestry division had sufficient information to prepare the billing statement in October or November 1986. The actual billing statement was prepared in November 1987. By not billing the U.S. Forest Service in a timely manner and not accruing the reimbursement amount to be received, General Fund revenue is understated in fiscal year 1986-87 by $49,824. The department lost an estimated $3,160 in interest earnings because the $49,824 was not requested and received in a timely manner. The department's untimely recording of federal reimbursements for fire suppression costs also understated revenue in fiscal years 1983-84 and 1984-85 as noted in our previous audit report.

According to state accounting policy, revenue should be recognized in the fiscal year in which it becomes measurable and available to finance expenditures of the accounting period. Recording the accrual at fiscal year-end would have ensured the reimbursement revenues were recorded in the same fiscal year that the related expenditures were recorded.

A department official indicated that due to an oversight, the department did not prepare the federal billing statement or accrue the revenue.

RECOMMENDATION #3

WE RECOMMEND THE DEPARTMENT:

A. PREPARE FEDERAL BILLING STATEMENTS IN A TIMELY MANNER.

B. RECOGNIZE REVENUE IN ACCORDANCE WITH STATE ACCOUNTING POLICY.

FIRE SUPPRESSION FUNDING

Responsibilities of the Department of State Lands include fire suppression on state and private land. Because of the unpredictable nature of fires, it is

difficult to budget fire suppression costs. The following paragraph describes the method of funding used at the present time.

The department pays the obligations incurred to control fires out of its General Fund budget. If the budget is not sufficient, the department must then request approval from the legislature for supplemental appropriations to fund the costs incurred in fighting the fires. The current arrangement functions adequately during the first year of the biennium since appropriation bills authorize transfer of spending authority from the second year of the biennium to the first without a supplemental appropriation. In the second year of the biennium, the department must request that the legislature grant a supplemental appropriation for payment of any unanticipated fire suppression costs incurred by the department during the biennium.

The current arrangement for fire suppression funding does not function adequately if during the second year of a biennium the fire season starts early and the legislature has adjourned. The department may not have sufficient General Fund appropriation authority to pay for its fire operations. As noted in our previous audit report, this situation occurred during June 1985. The legislature was not in session when a large fire broke out and General Fund appropriation authority was insufficient to pay the costs. As a result, the department incorrectly charged $212,000 incurred in fiscal year 1984-85 to fiscal year 1985-86 appropriations.

In our last two audit reports, we recommended the department investigate alternative methods of funding fire suppression and submit a proposed change to the Office of Budget and Program Planning with the department's next budget request. The funding alternatives discussed in the prior report included:

a) deficit spending authority;

b) treating state lands similar to private lands and assessing a fee to build a reserve;

c) providing a General Fund appropriation to be utilized for fire suppression when needed (i.e., emergency funds).

A department official indicated that the department had intended to request that the legislature enact a bill allowing deficit spending for fires occurring from the end of the legislative session to the end of the biennium.

However, due to an oversight, the official said the request for legislation was not made in the previous legislative session.

RECOMMENDATION #4

WE RECOMMEND THE DEPARTMENT DEVELOP AN IMPROVED METHOD OF FUNDING FIRE SUPPRESSION COSTS INCURRED AT THE END OF A BIENNIUM.

BOND SWAPS

To improve investment portfolios, the Board of Investments sometimes sells one security to provide funds for the purchase of another offering a higher yield. The original security is often sold at a loss. These transactions are referred to as "bond swaps."

Beginning in fiscal year 1985-86, the state began accounting for bond swaps related to the Trust and Legacy Fund on the state's accounting records in accordance with the completed transaction method. This procedure complies with the state law that requires the state's accounting records to reflect compliance with generally accepted accounting principles. However, when the state began accounting for bond swaps using the completed transaction method, the net loss from prior year bond swaps in the Trust and Legacy Fund was not addressed by the state. At June 30, 1987 the Trust and Legacy Fund corpus was impaired by $5.97 million as a result of prior year bond swap losses. Article X, Sections 3 and 10, Constitution of Montana, states that the funds of the educational institutions "... shall forever remain inviolate ..." The Montana Supreme Court in the case of In Re Montana Trust and Legacy Fund, stated that the rule of inviolability would not preclude the sale of securities at less than their purchase price with the intention of improving a portfolio. The justices interpreted the requirement that funds remain inviolate to mean that the principal could not be permanently impaired by direct application to educational purposes, or diversion to noneducational purposes. Based upon this interpretation, a temporary impairment of the Trust and Legacy Fund corpus resulting from losses on bond swaps does not violate the intent of Article X, Constitution of Montana.

Prior to fiscal year 1985-86 the state accounted for bond swap gains and losses using the deferral method of accounting. Use of the deferral method of accounting for bond swap losses restored the Trust and Legacy Fund corpus over a period of time. Therefore a system was in place to ensure losses to the Trust and Legacy Fund corpus were temporary and in accordance with provisions of the constitution.

When state accounting policy changed to the completed transaction method of accounting for bond swap losses, the department lost the system to ensure bond swap losses to the Trust and Legacy Fund corpus are only temporary. The department has not developed an alternative plan or system which would demonstrate that the trust fund impairment resulting from bond swap losses are in fact temporary, as required by the Montana Supreme Court interpretation of the constitution.

As of July 1, 1987, state policy requires administering agencies of trust funds to submit a plan for the restoration of fund balances to the Department of Administration, Accounting Division. Adoption of a plan by the Department of State Lands would ensure that the Trust and Legacy Fund corpus is restored.

RECOMMENDATION #5

WE RECOMMEND THE DEPARTMENT ADOPT A PLAN TO RESTORE THE TRUST AND LEGACY FUND CORPUS AS REQUIRED BY STATE POLICY.

FEDERAL REPORTS

The department did not accurately prepare two federal reports for its Abandoned Mine Lands Reclamation (AMLR) Program (CFDA #15.252). Federal regulations require that reports submitted to the federal government be accurate. We noted the June 1986 and the June 1987 Minority Business Enterprise Utilization Reports required by the AMLR program understated the total dollar value of each grant by $60,000 and $400,000, respectively. Department personnel indicated that due to an oversight the person preparing the reports did not use the amended grant agreements as a source for the information on the Minority Business Enterprise Utilization Report. If the department had an established review procedure to ensure federal reports are

accurate, the errors could have been detected and corrected before submission of the reports.

RECOMMENDATION #6

WE RECOMMEND THE DEPARTMENT ESTABLISH PROCEDURES TO ENSURE FEDERAL REPORTS ARE ACCURATE.

AUDITOR'S OPINION LETTER
AND AGENCY FINANCIAL SCHEDULES

SUMMARY OF AUDIT OPINION

The financial schedules are prepared from the Statewide Budgeting and Accounting System without adjustments for errors noted during the audit. The auditor's opinion issued in this report is intended to convey to the reader of the financial schedules the degree of reliance which can be placed on the amounts presented. The reader may rely on the fairness of the amounts presented.

STATE OF MONTANA

Office of the Legislative Auditor

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HELENA, MONTANA 59620
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SCOTT A. SEACAT
LEGISLATIVE AUDITOR

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FINANCIAL COMPLIANCE AUDITS
JIM PELLEGRINI
PERFORMANCE AUDITS

LEGAL COUNSEL:
JOHN W. NORTHEY

The Legislative Audit Committee
of the Montana State Legislature:

We have examined the financial schedules of the Department of State Lands for each of the two fiscal years ended June 30, 1986 and 1987 as shown on pages 12 through 20. Our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

As described in Note 1 to the financial schedules, the department's financial schedules are prepared in accordance with state accounting policy. Accordingly, the accompanying financial schedules are not intended to present financial position and results of operations in conformity with generally accepted accounting principles.

In our opinion, the financial schedules referred to above present fairly the results of operations of the Department of State Lands for the fiscal years ended June 30, 1986 and 1987 in conformity with the basis of accounting described in Note 1, which except for the changes in the recording of bond swap losses and the recording of revenue in the Nonexpendable Trust Fund (see Notes 5A and 12 to the financial schedules), with which we concur, have been applied on a consistent basis.

Respectfully submitted,

James Gillett

James Gillett, CPA
Deputy Legislative Auditor

November 6, 1987

DEPARTMENT OF STATE LANDS
SCHEDULE OF CHANGES IN FUND BALANCES
FOR THE TWO FISCAL YEARS ENDED JUNE 30, 1987

	General Fund	Special Revenue Funds	Capital Project Funds	Internal Service Funds	Nonexpendable Trust Fund
FUND BALANCE: July 1, 1985	$ -0-	$ 26,307,712	$26,936	$167,678	$229,491,577
ADDITIONS					
Fiscal Year 1986					
Budgeted Revenue & Transfers In	272,186	45,867,821		183,182	9,214,460[4]
Prior Year Revenue Adjustments	529,681[2]	4,598,145[2]			243,096
Support From State Of Montana	7,886,818				
Nonbudgeted Revenue & Transfers In					2,347,086
Cash Transfer In					455,669
Fiscal Year 1987					
Budgeted Revenue & Transfers In	215,373	46,531,119		151,538	
Nonbudgeted Revenue & Transfers In	3,377,750[1]				10,194,269[4]
Support From State Of Montana	3,259,698				
Cash Transfers In			20,905		381,992
Total Additions	15,541,506	96,997,085	20,905	334,720	22,836,572
REDUCTIONS					
Fiscal Year 1986					
Budgeted Expenditures & Transfers Out	8,678,725	10,256,379		197,587	
Prior Year Expenditure Adjustments	9,960	(99,002)		9,140	
Cash Transfers Out		33,875,743	8,661		
Nonbudgeted Expenditures & Transfers Out				675	224,798
Direct Entries To Fund Balance[3]					9,204,590
Fiscal Year 1987					
Budgeted Expenditures & Transfers Out	6,844,605	11,064,532	22,941	179,537	
Prior Year Expenditure Adjustments	8,216	41,133		5,986	
Cash Transfer Out		37,181,676			
Prior Year Expenditures		452			
Nonbudgeted Expenditures & Transfers Out				1,277	50,810
Direct Entries To Fund Balance[3]					23,449
Total Reductions	15,541,506	92,320,913	31,602	394,202	9,503,647
FUND BALANCE: June 30, 1987	$ -0-	$30,983,884	$16,239	$108,196	$242,824,502

[1]See Note 8 on page 19.
[2]See Note 9 on page 19.
[3]See Note 5 on page 18.
[4]See Note 12 on page 20.

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules on pages 16 through 20.

DEPARTMENT OF STATE LANDS
SCHEDULE OF BUDGETED REVENUE & TRANSFERS IN - ESTIMATED & ACTUAL
FOR THE TWO FISCAL YEARS ENDED JUNE 30, 1987

	Licenses and Permits	Charges For Services	Investment Earnings	Federal Indirect Cost Recoveries	Taxes	Fines & Forfeits	Sale of Documents & Merchandise	Rentals, Leases & Royalties	Miscellaneous	Grants, Contracts, Donations	Federal	Total
Fiscal Year 1987												
GENERAL FUND												
Estimated Revenue	$ 5,000	$ 210,000	$ 6,450	$ 21,296								$ 242,746
Actual Revenue	5,521	187,638	0	22,214								215,373
Collections Over (Under) Estimate	$ 521	$ (22,362)	$ (6,450)	$ 918								$ (27,373)
SPECIAL REVENUE FUND												
Estimated Revenue	$10,000	$ 956,000	$34,225,000	$ 88,704	$1,057,000	$ 2,000	$ 110,000	$ 300,000	$102,000	$ 10,000	$ 7,338,563	$44,199,267
Actual Revenue	6,160	932,465	35,521,216	92,527	1,054,591	7,500	138,551	394,314	59,404	73,279	8,251,112	46,531,119
Collections Over (Under) Estimate	$(3,840)	$ (23,535)	$ 1,296,216	$ 3,823	$ (2,409)	$ 5,500	$ 28,551	$ 94,314	$(42,596)	$ 63,279	$ 912,549	$ 2,331,852
INTERNAL SERVICE FUNDS												
Estimated Revenue		$ 170,000										$ 170,000
Actual Revenue		151,538										151,538
Collections Over (Under) Estimate		$ (18,462)										$ (18,462)
Fiscal Year 1986												
GENERAL FUND												
Estimated Revenue	$ 2,000	$ 205,000	$ 65,000	$ 29,700								$ 301,700
Actual Revenue	6,341	219,009	15,275	31,561								272,186
Collections Over (Under) Estimate	$ 4,341	$ 14,009	$(49,725)	$ 1,861								$ (29,514)
SPECIAL REVENUE FUND												
Estimated Revenue	$ 7,000	$1,049,455	$36,220,000	$140,300	$ 1,004,039	$ 37,000	$ 120,852	$ 570,000	$ 69,000	$ 765,732	$ 7,912,710	$47,896,088
Actual Revenue	12,115	446,608	37,351,172	287,964	1,009,359	342,071	122,570	403,233	23,296	257,387	5,612,046	45,867,821
Collections Over (Under) Estimate	$ 5,115	$ (602,847)	$ 1,131,172	$147,664	$ 5,320	$305,071	$ 1,718	$ (166,767)	$(45,704)	$(508,345)	$(2,300,664)	$(2,028,267)
INTERNAL SERVICE FUNDS												
Estimated Revenue		$ 154,257										$ 154,257
Actual Revenue		183,182										183,182
Collections Over (Under) Estimate		$ 28,925										$ 28,925
NONEXPENDABLE TRUST FUNDS[1]												
Estimated Revenue			$ 1,900,000				$1,715,100	$ 8,022,700			$ 20,000	$11,657,800
Actual Revenue			1,963,215				1,091,234	6,148,265			11,746	9,214,460
Collections Over (Under) Estimate			$ 63,215				$ (623,866)	$(1,874,435)			$ (8,254)	$(2,443,340)

[1]See Note 12 on page 20.

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules on pages 16 through 20.

DEPARTMENT OF STATE LANDS
SCHEDULE OF BUDGETED PROGRAM EXPENDITURES BY OBJECT AND FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 1987

	Central Management	Reclamation	Land Administration	Resource Development	Forestry	Total
PERSONAL SERVICES						
Salaries	$ 463,242	$ 755,181	$358,147	$157,593	$3,487,820	$ 5,221,983
Hourly Wages					985,830	985,830
Employee Benefits	94,511	151,966	75,675	32,197	886,135	1,240,484
Total	557,753	907,147	433,822	189,790	5,359,785	7,448,297
OPERATING EXPENSES						
Contracted Services	361,308	2,503,566	18,347	14,062	787,705	3,684,988
Supplies & Materials	44,086	38,314	17,335	3,384	506,495	609,614
Communications	16,920	34,703	20,929	3,475	145,931	221,958
Travel	9,973	89,976	18,545	6,273	73,335	198,102
Rent	67,475	97,485	4,583	11,171	336,381	517,095
Utilities	11,881	6,521	925	931	70,899	91,157
Repair & Maintenance	118,672	8,516	6,792	580	305,625	440,185
Other Expenses	3,354	70,906	2,473	3,169	26,935	106,837
Total	633,669	2,849,987	89,929	43,045	2,253,306	5,869,936
EQUIPMENT AND INTANGIBLE ASSETS						
Equipment	32,086	31,521			77,234	140,841
Total	32,086	31,521			77,234	140,841
CAPITAL OUTLAY						
Land & Interest In Land		4,384,790		1,212		4,386,002
Other Improvements				6,839		6,839
Total		4,384,790		8,051		4,392,841
GRANTS						
From State Sources	259,700					259,700
Total	259,700					259,700
TOTAL PROGRAM EXPENDITURES	$1,483,208	$8,173,445	$523,751	$240,886	$7,690,325	$18,111,615
GENERAL FUND						
Budgeted	$ 850,435	$ 520,474	$517,348		$4,980,076	$ 6,868,333
Actual	839,863	513,367	517,212		4,974,163	6,844,605
Unspent Budget Authority	$ 10,572	$ 7,107	$ 136		$ 5,913	$ 23,728
SPECIAL REVENUE FUND						
Budgeted	$ 567,665	$8,997,050	$ 7,000	$593,113	$3,263,735	$13,428,563
Actual	463,808	7,660,078	6,539	240,886	2,693,221	11,064,532
Unspent Budget Authority	$ 103,857	$1,336,972	$ 461	$352,227	$ 570,514	$ 2,364,031
INTERNAL SERVICE FUNDS						
Budgeted	$ 196,146					$ 196,146
Actual	179,537					179,537
Unspent Budget Authority	$ 16,609					$ 16,609
CAPITAL PROJECTS FUNDS						
Budgeted					$ 44,000	$ 44,000
Actual					22,941	22,941
Unspent Budget Authority					$ 21,059	$ 21,059

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules on pages 16 through 20.

DEPARTMENT OF STATE LANDS
SCHEDULE OF BUDGETED PROGRAM EXPENDITURES BY OBJECT AND FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 1986

	Central Management	Reclamation	Land Administration Program	Resource Development Program	Forestry	Total
PERSONAL SERVICES						
Salaries	$ 459,719	$ 874,095	$313,961	$146,964	$ 3,227,531	$ 5,022,270
Hourly Wages			3,609		1,063,976	1,067,585
Employee Benefits	91,552	174,182	65,285	29,997	813,603	1,174,619
Total	551,271	1,048,277	382,855	176,961	5,105,110	7,264,474
OPERATING EXPENSES						
Contracted Services	273,128	2,060,676	13,371	10,181	2,877,237	5,234,593
Supplies & Materials	51,761	34,909	25,203	3,281	766,958	882,112
Communications	18,519	43,469	27,284	4,657	156,592	250,521
Travel	14,876	93,614	20,592	7,361	86,070	222,513
Rent	72,928	121,167	8,616	4,815	479,919	687,445
Utilities	9,441	5,909	151	711	82,893	99,105
Repair & Maintenance	145,938	13,156	8,126	1,844	349,889	518,953
Other Expenses	1,892	121,977	2,818	290,436	46,768	463,891
Total	588,483	2,494,877	106,161	323,286	4,846,326	8,359,133
EQUIPMENT AND INTANGIBLE ASSETS						
Equipment	3,342	34,446	56,939	429	585,026	680,182
Intangible Assets		358			6,672	7,030
Total	3,342	34,804	56,939	429	591,698	687,212
CAPITAL OUTLAY						
Land & Interest In Land		2,540,531		4,100		2,544,631
Other Improvements				12,241		12,241
Total		2,540,531		16,341		2,556,872
GRANTS						
From State Sources	265,000					265,000
Total	265,000					265,000
TOTAL PROGRAM EXPENDITURES	$1,408,096	$6,118,489	$545,955	$517,017	$10,543,134	$19,132,691
GENERAL FUND						
Budgeted	$ 874,701		$553,330		$ 7,340,800	$ 8,768,831
Actual	845,053		545,955		7,287,717	8,678,725
Unspent Budget Authority	$ 29,648		$ 7,375		$ 53,083	$ 90,106
SPECIAL REVENUE FUND						
Budgeted	$ 644,967	$9,297,070		$584,737	$ 4,051,603	$14,578,377
Actual	365,456	6,118,489		517,017	3,255,417	10,256,379
Unspent Budget Authority	$ 279,511	$3,178,581		$ 67,720	$ 796,186	$ 4,321,998
INTERNAL SERVICE FUNDS						
Budgeted	$ 212,332					$ 212,332
Actual	197,587					197,587
Unspent Budget Authority	$ 14,745					$ 14,745
CAPITAL PROJECTS FUNDS						
Budgeted					$ 44,000	$ 44,000
Actual					-0-	-0-
Unspent Budget Authority					$ 44,000	$ 44,000

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provid
in the notes to the financial schedules on pages 16 through 20.

MONTANA DEPARTMENT OF STATE LANDS

NOTES TO THE FINANCIAL SCHEDULES

FOR THE TWO FISCAL YEARS ENDED JUNE 30, 1987

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Basis of Accounting

The state of Montana utilizes the modified accrual basis of accounting which is described in the Montana Operations Manual.

Under the modified accrual basis of accounting, expenditures are recorded for valid obligations. A valid obligation exists when the related liability is incurred except for the following items which are also considered valid obligations under state accounting policy.

- If the appropriation provided funds to complete a given project, the entire amount of a contract may be accrued even though the services are rendered in fiscal years subsequent to the fiscal year in which the expenditure is accrued.
- The anticipated cost of equipment is accrued in the fiscal year in which budgeted.
- Goods ordered, but not received as of the fiscal year-end may be accrued if the purchase order was issued in the fiscal year in which the anticipated expenditure is to be accrued.

Revenues are recorded when received in cash unless susceptible to accrual. Revenues are susceptible to accrual if they are measurable and available to finance expenditures of the fiscal period.

The Department of State Lands uses the accrual basis of accounting for Proprietary and Nonexpendable Trust Funds. Under the accrual basis of accounting, revenues are recognized in the accounting period in which they are earned; expenses are recognized in the period incurred.

B. Basis of Presentation

The financial schedules were prepared from the Statewide Budgeting and Accounting System (SBAS) without adjustments. Accounts are organized on the

basis of funds according to state law. The following funds are used by the department:

General - accounts for all financial resources except those required to be accounted for in another fund. Activities of the central management, land, administration, and forestry programs are partially recorded in the General Fund.

Special Revenue - accounts for the proceeds of specific revenue sources that are legally restricted to expenditures for specified purposes. Legislative appropriations are required to be spent from this fund. Activities in this fund include federal funds received by the department plus funds for land development, reclamation, and forestry.

Capital Projects - accounts for financial resources to be used for the acquisition or construction of major capital facilities.

Internal Service - accounts for the financing of goods or services provided by one department or agency to other departments or agencies of the governmental unit, or to other governmental units, on a cost-reimbursement basis. This fund reflects the financial activities of the air operations bureau.

Nonexpendable Trust - accounts for assets held by a governmental unit in a trustee capacity or as an agent for individuals, private organizations, other governmental units, and/or other funds. This fund includes the permanent trust funds established by the constitution as permanent income sources for the university units, public schools, and institutions.

2. ANNUAL AND SICK LEAVE

Employees at the department accumulate both annual and sick leave. Employees are paid for 100 percent of unused annual and 25 percent of unused sick leave credits upon termination. Accumulated unpaid liabilities for annual and sick leave are not reflected in the financial schedules of the Department of State Lands. Expenditures for termination pay currently are absorbed in the annual operational costs of the department. At June 30, 1987, the department had an approximate liability of $525,000 for annual leave and $325,500 for sick leave.

3. PENSION PLAN

Employees are covered by the Montana Public Employees' Retirement System (PERS). The department's contribution to this plan was $356,500 in fiscal year 1985-86 and $366,500 in fiscal year 1986-87.

4. GENERAL FUND BALANCE

The General Fund is a Statewide Fund. Agencies do not have a separate General Fund since their only authority is to pay obligations from the Statewide General Fund as long as they stay within their appropriation limits. Thus, on an agency schedule, the beginning and ending fund balance will always be zero for the General Fund.

5. DIRECT ENTRIES TO FUND BALANCE

Nonexpendable Trust Fund -

A. In fiscal year 1985-86, this entry records the cumulative effect of bond swap losses using the completed transaction method of accounting. Bond swap losses were previously recorded using the deferral method of accounting. Beginning in fiscal year 1985-86, state policy requires agencies to apply the completed transaction method of accounting. The cumulative effect of bond swap losses represented a $9.2 million impairment of Trust and Legacy Fund corpus as of July 1, 1985. Due to bond swap gains during fiscal year 1985-86 and fiscal year 1986-87, the impairment of Trust and Legacy Fund corpus was reduced to $5.97 million at June 30, 1987.

B. In fiscal year 1986-87, the direct entry to fund balance represents the transfer of donated moneys to the Department of Institutions. The moneys were donated for the benefit of certain institutions but were invested by and accounted for at the Department of State Lands, based upon state law. Due to a change in state law, the Department of Institutions is now allowed to account for the donated moneys.

6. CASH TRANSFERS

Under the Statewide Budgeting and Accounting System (SBAS), several state agencies may record activity in the same accounting entity. During the fiscal year, the activity for each agency is recorded on SBAS separately. At the end of the fiscal year, the activity for all the agencies using the accounting entity is combined on SBAS in a combined accounting entity. The

cash transfers reflected on the Schedule of Changes in Fund Balance represent the fiscal year-end transfer of the cash balances in the department's combining accounting entities to or from the state's combined accounting entities.

7. NONEXPENDABLE TRUST FUNDS

The nonbudgeted expenditures and transfers out in this fund in fiscal year 1986-87 represent a temporary loss of corpus on bond swap transactions.

8. MONTANA YOUTH TREATMENT CENTER

The General Fund nonbudgeted revenue and transfers-in reported in fiscal year 1986-87 represent the proceeds from the sale of the Montana Youth Treatment Center located in Billings, Montana.

9. PRIOR YEAR REVENUE ADJUSTMENTS

General Fund - In fiscal year 1985-86, the department received reimbursement for fiscal year 1984-85 fire suppression costs from the Federal Emergency Management Agency (FEMA).

Special Revenue Fund - Beginning in fiscal year 1985-86, state policy required state agencies to accrue investment earnings on SBAS at fiscal year-end. The prior year revenue adjustment represents the recording of the fiscal year 1984-85 investment accrual in accordance with state policy.

10. PROGRAM EXPENDITURES

Forestry - the contracted services expenditures in fiscal year 1985-86 are predominantly fire suppression costs incurred during an active fire season.

Resource Development - the "other expenses" reported in fiscal year 1985-86 represent the payment of special improvement district taxes on state lands.

11. UNSPENT BUDGET AUTHORITY

The budgeted expenditures reported in the reclamation program are primarily related to federally funded projects on abandoned mine land. Actual expenditures depend upon the number and dollar amount of federal projects and may vary between fiscal years. In fiscal year 1985-86, the actual federal project expenditure activity was less than anticipated, resulting in unspent budget authority.

12. CHANGES IN ACCOUNTING

In fiscal year 1985-86, most of the nonexpendable trust fund revenue was recorded as budgeted. Beginning in fiscal year 1986-87, all nonexpendable trust fund revenue is recorded as nonbudgeted.

AGENCY RESPONSE

DEPARTMENT OF STATE LANDS

TED SCHWINDEN GOVERNOR

CAPITOL STATION

STATE OF MONTANA

(406) 444 2074

1625 ELEVENTH AVENUE
HELENA, MONTANA 59620

APR 11 1988
MONTANA LEGISLATIVE

April 5, 1988

Mr. Scott A. Seacat
Legislative Auditor
State Capitol
Helena, Montana 59620

Dear Mr. Seacat:

Attached is the Department of State Lands response to the audit report for the fiscal years ending June 30, 1987. I believe the responses are complete, however if you or your staff have any questions, please feel free to contact me.

Sincerely,

Dennis Hemmer
Commissioner

ATTACH:

AN EQUAL OPPORTUNITY EMPLOYER

AGENCY RESPONSE TO AUDIT RECOMMENDATIONS

Recommendation #1
The department continue to request advance payments from the federal government.

Agency Response
Concur

Explanation
In the 1983 Legislature the agency requested funds for automation of its records explaining that revenue was being lost by not being able to deposit funds in a timely fashion. The Legislature denied the request and deleted two positions used for central management functions over the agency's objections. In 1985 the agency again requested funds to automate its records. The Legislature authorized the agency to use Resource Development funds to automate its records however it also funded a portion of the timber harvest from Resource Development funds. There were insufficient funds and therefore both were reduced. In 1987 the Legislature approved funds to complete automation of the ownership records (a prerequisite to automating the payment function) and payments. The payment automation was activated January 1, 1988.

Prior to Farm Program signup for the 1987 crop year the agency's antiquated manual cashiering system and staffing did not allow for the acceptance of advance payments. It was difficult to handle the Farm Program payments at all let alone a second set. For the 1987 crop year the agency "patched together" a combination of an old automated record system and the manual system which allowed it to accept advance payments. While the system allowed the acceptance of payments it also created a lot of problems for lessees due to erroneous reports.

The process put in place to allow the acceptance of advance payments was begun at the agency's initiative before the issue was flagged to the Legislative Auditor.

Implementation/Corrective Action
None is required as the system is in place.

Recommendation #2
The department record all expenditures and liabilities for insurance premiums in the year incurred.

Agency Response
Concur

Explanation
The agency felt that House Bill 500 allowed it to pay only the amount it was authorized by the Legislature. The agency felt that House Bill 500 directed that the rest of the payment be made by the Department of Administration

Implementation/Corrective Action
The agency will pay its insurance bills.

Recommendation #3
The department:
A. Prepare federal billing statements in a timely manner.

B. Recognize revenue in accordance with state accounting policy.

Agency Response
Concur

Implementation/Corrective Action
The agency has implemented measures to correct the problem.

Recommendation #4
The department develop an improved method of funding fire suppression costs incurred at the end of a biennium.

Agency Response
Concur

Implementation/Corrective Action
The Department will ask the 1989 Legislature for deficit spending authority for those fires occurring after the Legislature meets, but before the beginning of the next fiscal year.

Recommendation #5
The department adopt a plan to restore the trust and legacy fund corpus as required by state policy.

Agency Response
Concur

Implementation/Corrective Action
Beginning in fiscal year 1988 the Department will amortize gains and losses from bond swaps over the shorter of either the remaining life of the bonds sold or the replacement bonds purchased. Beginning in fiscal year 1988 the Department will deposit from the distributable income an amount equal to 10% of the amount not amortized for the last two fiscal years.

Recommendation #6
The department establish procedures to ensure federal reports are accurate.

Agency Response
Concur

Implementation/Corrective Action
The agency will endeavor to make sure all federal reports are accurate.